

This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 02 CAIRO 008161

SIPDIS

SENSITIVE

STATE FOR NEA/ELA, NEA/RA, AND EB/IDF
USAID FOR ANE/MEA MCCLLOUD
USTR FOR SAUMS
TREASURY FOR MILLS/NUGENT/PETERS
COMMERCE FOR 4520/ITA/ANESA/TALAAAT

E.O. 12958: N/A

TAGS: [ECON](#) [EFIN](#) [EINV](#) [EIND](#) [EG](#)

SUBJECT: GOE PRIVATIZES "STRATEGIC" FIRMS, WITHIN LIMITS

This message is not for Internet distribution.

Summary

1. (SBU) The Ministry of Investment (MOI) has recently acted to extend the revitalized privatization program to cover petrochemical firms, which were previously considered untouchable "strategic" companies, theoretically important to Egypt's overall economic security. Nevertheless, there remain limits as to what the Nazif Cabinet, through Minister of Investment Dr. Mahmoud Mohieldin, can do on strategic enterprises, as demonstrated by the retention of key fertilizer-producing companies. Concerns over the social and economic impact of privatizations - especially with parliamentary elections on the immediate horizon - provide a check on the program, the MOI's protestations notwithstanding. End summary.

The Petrochemicals Wave

2. (U) In the past few months the MOI has floated 20% of shares in two very profitable joint venture firms (JVs) in the energy sector, Sidi Krir Petrochemicals Co. (SIDPEC) and Alexandria Mineral Oil Company (AMOC). SIDPEC is Egypt's largest producer of ethylene and polyethelene, while AMOC, though accounting for only 2% of Egypt's total refinery output, operates two modern complexes for mineral oils and paraffin wax production. Both initial public offerings (IPOs) were greatly oversubscribed; the two tranches of SIDPEC shares put on the market were oversubscribed by 2.5 and 5 times, respectively, while for AMOC, overselling reached 26% and 34% for the two consecutive tranches. (Note: While the over-subscription is indicative of the attractiveness of these firms, it should be taken in context. Stock market mechanisms in Egypt allow limitless calls for shares with only a small amount required to be paid upfront. End note.)

3. (SBU) The two IPOs not only stimulated the stock market but also contributed to growth in privatization proceeds, which reached LE 5.1 billion during the first quarter of FY 2006 (July to September) alone. The June SIDPEC offering topped out at 21.0 million shares at LE 70 per share, for a total value of LE 1.5 billion; mid-September sales of AMOC stock came to 86.1 million shares at LE 45 per share, for a total of LE 900 million. In a recent meeting with Econoff, Mohamed Hassouna, Advisor for Public Enterprises to the Minister of Investment, revealed that given the success of the IPOs, the GOE will soon offer shares in yet a third petrochemical firm, Middle East Oil Refinery (MIDOR).

4. (SBU) Hassouna explained that the sales technique introduced by the MOI for these JVs, and others to follow, involves floating 20-30% of shares on the stock market, and then selling 50-60% to an anchor investor, while retaining 20% for the GOE. Minister of Investment Mohieldin believes this approach serves the dual aims of stimulating the stock market and improving management of the companies through sale to a major investor. Citibank and the National Bank of Egypt have already been chosen as promoters for SIDPEC's anchor investor tender offering. Hassouna also described MOI's technique of "market sounding," i.e., making public statements regarding upcoming privatizations to get a sense of the market's reaction before actually making the IPOs. Hassouna believes this technique was partly responsible for the success of the petrochemical offers.

The Opposition

5. (SBU) MOI has not been immune to criticism over the sales, despite the success, from certain quarters. Al-Araby

newspaper, the mouthpiece of the nationalist, statist Nasserist Party, for instance, on September 25 complained that the GOE had opened the door for increased dominance by international capitalist enterprises over key industries. Aziz Sidky, Egypt's prime minister from 1972-1973 - the period during which the "public enterprises" were first created - similarly expressed dismay. MOI responded to the criticism by insisting that profitable sales are not only important for the companies' future viability but are also economically justifiable in the near term.

16. (SBU) The overriding concern for MOI, whether in the petrochemical industry or elsewhere, remains labor opposition. According to Hassouna, Mohiieldin regularly meets with labor unions and labor representatives on the boards of directors of public sector companies. Unlike in previous years, MOI also includes labor representatives in the actual privatization negotiations with potential investors. In most cases, workers are offered excellent early retirement packages if downsizing is a part of the negotiations. Hassouna opined that workers frequently object to privatization on principle without understanding the mechanics; once they begin to understand the mechanics and realize that they will not be dismissed without any compensation, they generally stand down on their opposition.

"Strategic" Sectors Remain: the Case of Fertilizers

17. (SBU) Domestic social and economic considerations still put a damper on the prospects for privatization of some industries, despite statements from MOI that "nothing is off the table." A case in point is the fertilizer sector, which, according to Hassouna, foreign investors - especially from India and China - have been eyeing for some time. Hassouna stated that the GOE fears damage to domestic agricultural production if foreign investors take charge of the fertilizer sector and begin exporting the bulk of Egypt's fertilizer output. For this reason, three "core" fertilizer companies - KIMA, Delta and Al-Nasr Mining - will not be entirely privatized but will remain a "safety valve" (Hassouna noted that Mohiieldin strongly resists using the term "strategic"), although there are plans to offer up 20-30% of Al-Nasr, which holds the monopoly over phosphate quarries.

18. (SBU) Mohiieldin has also set up a Sectoral Study Committee to probe the possibility of deregulating the fertilizer industry. (Comment: Setting up the committee is likely a means to pay lip service to the "nothing is off the table" concept. End comment.) Asian investors interested in the fertilizer sector have not been put off entirely, and have actually established greenfield fertilizer projects in Egyptian free zones. Several Asian producers recently signed an MOU with Al Nasr Mining Co. to supply the raw material needed in these greenfield projects. One hundred percent of the output of these projects is exported to Asia.

Comment

19. (SBU) Mohiieldin said recently in an interview with the Oxford Business Group "privatization is one of the components - not the component - of reform." This was likely an effort to curb public suspicion that the GOE plans to give away the store to foreigners, unmindful of dangers to labor and economic security. The Minister claimed he did not fear innovation in the Egyptian privatization program - or, as he has re-dubbed it, the "asset management program." He claimed that innovation has contributed to smoothing out many bumpy parts in the privatization process. Nevertheless, even as he touches previously untouchable industries, Mohiieldin claims he will moderate the pace of privatization and work hard to manage expectations. We would be surprised if the MOI were to pull off any more controversial privatization deals prior to next month's parliamentary elections. End comment.